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TRADE AND DEVELOPMENT BOARD
Commission on Enterprise, Business
Facilitation and Development
Meeting of Experts on Government and Private
Sector Roles and Interactions for SME Development
Geneva, 23-25 July 1997
Item 2 of the provisional agenda

PROVISIONAL AGENDA AND ANNOTATIONS

I. Provisional agenda

1. Election of officers

2. Adoption of the agenda

3. The respective roles of government and the private sector, including NGOs, and the interactions between them in creating a coherent policy framework and setting up effective support measures and structures for the development of SMEs and micro-enterprises, in particular those in least developed countries

4. Adoption of the report.

GE.97- 5I037

II. Annotations to the provisional agenda

Item 1 - Election of officers

It is recommended that the Expert Meeting elect a Chairman and a Vice-Chairman-cum-Rapporteur.

Item 2 - Adoption of the agenda

The provisional agenda for the Meeting is in section I above. The draft schedule of meetings for the three days is attached to this document.

Documentation

TD/B/COM.3/EM.2/1	Provisional agenda and annotations

Item 3 - The respective roles of government and the private sector, including NGOs, and the interactions between them in creating a coherent policy framework and setting up effective support measures and structures for the development of SMEs and micro-enterprises, in particular those in least developed countries;

With a view to expediting substantive discussions of the Expert Meeting, the secretariat has prepared an issues paper entitled "Government-private sector interaction, with a particular focus on the participation of SMEs" (TD/B/COM.3/EM.2/2).

The paper attempts to respond to the request expressed by the Commission on Enterprise, Business Facilitation and Development at its first session by indicating the main issues involved in promoting effective government-private sector interaction for the development of SMEs. It raises and discusses major policy issues which can be the subject of useful cross-country exchanges of lessons learned and insights gained from national experiences in conducting an effective government-private sector dialogue with a view to achieving better policy coherence for the development of SMEs and to promoting support mechanisms and services for SMEs.

The deliberations of the Expert Meeting under this substantive item are expected to help the Commission to draw lessons from country experiences and to identify "best practices" that can contribute to the improvement of the policy and institutional environment for enterprise development, particularly for SMEs. The exchange of lessons and experiences in the Expert Meeting may also assist governments in preparing country presentations for the second session of the Commission on Enterprise, Business Facilitation and Development.

Documentation

TD/B/COM.3/EM.2/2	"Government-private sector interaction, with a particular focus on the participation of SMEs"

Item 4 - Adoption of the report

The Expert Meeting will adopt its recommendations and conclusions at the end of the Meeting. The final report will be compiled under the authority of the Chairman after the conclusion of the Meeting.

Draft schedule of meetings

Day 1	Day 2	Day 3
AM Plenary: Director opening Elections/agenda Informals: Substantive item 3	AM Informals (cont'd): Substantive item 3	AM Informals (cont'd): Consideration of draft text (recommendations)
PM Informals (cont'd): Substantive item 3	PM Informals (cont'd): Substantive item 3	PM Informals (cont'd): Consideration of draft text (recommendations) (cont'd) Plenary (closing) Adoption of the report

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Commission on Enterprise, Business
Facilitation and Development
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Geneva, 23-25 July 1997
Item 3 of the provisional agenda

Government-private sector interaction, with a particular focus on the participation of SMEs

Issues paper by the UNCTAD secretariat

GE.97-50887 (E)

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I. Preface

1. The Commission on Enterprise, Business Facilitation and Development agreed at its first session, which took place from 20 to 24 January 1997, that further policy research within UNCTAD would be needed in particular areas related to the promotion of SMEs. It also took note of the proposals for relevant issues for analytical work and intergovernmental discussion made in this regard, including, inter alia, "the respective roles of government and the private sector, including NGOs, and the interactions between them in creating a coherent policy framework and setting up effective support measures and structures for the development of SMEs and micro-enterprises, in particular those in least developed countries". 1/

2. In light of the above considerations, the Commission decided to convene an Expert Meeting on this topic. 2/

3. This paper attempts to respond to the request expressed by the Commission by indicating the main issues involved in promoting effective government-private sector interaction, including the achievement of policy coherence and the establishment of effective support structures and services for SME development. In each case, a brief outline of the main issues is given, followed by a set of related questions which may help experts to prepare their contributions in order to facilitate and enrich the exchange of country experiences. The expert contributions would help the Commission to draw lessons from country experiences and to identify "best practices" that can contribute to the improvement of the policy and institutional environment for enterprise development, particularly for SMEs.

4. This Expert Meeting is part of a longer-term intergovernmental process addressing issues related to the formulation and implementation of enterprise development strategies. Other issues such as networking, geographical clustering, technological capacity-building and innovation policies may be explored in future expert meetings.

II. The setting

5. The twin processes of globalization and liberalization, combined with rapid advances in information and communications technologies, are creating new dynamics of production, enterprise development and of international competition. These changes, in turn, call for a holistic and integrated approach to enterprise development that addresses the multiplicity and interaction of factors that underpin the growth and competitiveness of enterprises. They also imply the need for countries to formulate enterprise development strategies, which take into account the role of the private sector and the role of the State, as well as the interaction between them. However, all these activities, of both the private and public sectors, in order to have maximum usefulness and impact, will need to take place within a coherent policy framework, involving cooperation and dialogue between the government and the private sector, including representatives of small and medium-sized enterprises (SMEs).

6. SMEs have become essential actors in the development process in both developing countries and economies in transition. Their large number (accounting for more than 90 per cent of all enterprises in the vast majority of countries) and their involvement in a wide variety of activities, ranging from providing goods and services to the poor, to the manufacture of exports, underline the particular economic and social importance of SMEs. SMEs provide a breeding ground for entrepreneurs. Through the "demonstration" effect, they spawn new enterprises. They are also able to use resources that may otherwise not be drawn into the development process. By encouraging personal savings and the use of the retained savings of firms, they also play an important role in mobilizing and generating domestic savings.

7. Often SMEs are at the forefront of technological change and innovation. Their relatively small size enhances their need, as well as their capacity, to adapt to change. They are condemned to be innovative and competitive in order to develop and to survive. They also need to be entrepreneurial in order to exploit new opportunities or new processes. They thus play an important part in generating greenfield investments and in expanding existing business activities into new areas. The development of software industries in India, the success of small-scale fashion industries in Hong Kong and in the Emilia-Romagna region of Italy, as well as the flourishing machine tool sector in Taiwan Province of China, are examples where SMEs have broken new ground and demonstrated their competitiveness in both domestic and international markets.

8. SMEs have a major impact on the social situation of a country. Because of their dynamism and flexibility, SMEs are crucial for the creation of new employment opportunities. In practically all countries, SMEs provide the majority of jobs. And, while large-scale enterprises tend to shed jobs, as in many developed countries where the trend towards labour shedding is a source of concern, SMEs continue to be the main, if not the only source, of new jobs, both in developed and developing countries. 3/ Nevertheless, the many positive contributions of SMEs have not always been appreciated.

9. As a precondition for successful enterprise development, particularly the promotion of SMEs, the government needs to establish the right macroeconomic environment, as well as a transparent, stable and predictable legal, regulatory and tax framework. As experience in East Asia for example suggests, even where it is least interventionist, the government still plays a key and fundamental role in terms of providing a facilitating policy and institutional environment for enterprise development. Further, it can stimulate, facilitate or support the development and internationalization of enterprises, particularly SMEs, by acting as a catalytic or intermediating agent and by adopting appropriate measures, such as programmes for SME financing, for providing business support services such as quality control and productivity improvement, for facilitating networking and clustering through, for example, network brokers or subcontracting exchanges, for facilitating the commercialization of R&D through, for example, technology incubators, and for assisting first-time exporters. Governments always have a choice regarding policy intervention, for example as between functional intervention, such as reducing the regulatory burden on all businesses, or selective intervention such as easing particular regulations for SMEs, and need to weigh their costs and benefits, including any related externalities. 4/

10. By developing the necessary physical infrastructure, knowledge and skills, including in cooperation with the private sector, as well as providing appropriate incentives, the government can promote innovative capacity and structural change in the economy. In cooperation with the private sector, it can also use the educational system to produce job creators rather than job seekers. 5/ In addition, together with other Governments, it can help to promote regional cooperation, for example by encouraging the networking of SME support agencies, in order to undertake joint activities and to pool resources such as in the area of business support services, as well as to foster inter-firm cooperation.

11. The government can also work with other governments in order to create "growth triangles" linking contiguous areas in production and trade cooperation, as well as in the development of infrastructure. Such cooperative arrangements combine the benefits of both clustering and networking.

12. Experience has shown that, in the absence of a coherent policy environment, the globalization of production and the opening of domestic markets as part of liberalization policies or of structural adjustment programmes has had adverse effects on the enterprise structure, particularly the SME sector, in many least developed countries in Africa, as well as in some other developing countries. These consequences have led to a situation where SMEs have been massively destroyed or are continually losing ground in terms of their competitiveness, giving rise to a missing or declining middle in the enterprise structure in these countries, accompanied by a corresponding expansion of the micro-enterprise or survival sectors of the economy.

13. Given the importance of SMEs, these trends can have serious implications for the economic and social development of these countries in terms of its effects on income and earnings distribution, the tax and consumption base and the ability of the economy to modernize and integrate itself into the global economy. The process may also become self-reinforcing in the sense that reduced demand (compounded by the impact of higher interest rates of structural adjustment policies) and falling tax revenue may inhibit the ability of the State to help deserving SMEs when such help is most needed in order to enable them to survive and to adjust successfully. Some external transitional help to meet the cost of such SME support programmes may thus be needed. 6/

III. Government-private sector interaction

14. An effective interaction and dialogue between the government and the private sector, including NGOs, can play a key role in creating a coherent policy framework and effective support measures and structures for the development of SMEs. 7/ Since the private sector operates in a dynamic context and the government's role itself may evolve in response to changing circumstances and requirements, such a dialogue provides a forum to address the changes in a flexible and concerted manner and to formulate jointly proper measures and policies that meet government objectives and at the same time enjoy the support of the private sector.

15. Some form of government-private sector interaction exists in virtually all countries - at various levels of government, including regional and local administrations, and sometimes for particular sectors. However, in many developing countries and economies in transition, contacts between the government and the private sector are often informal, spontaneous, partial or unstructured. Further they often lack transparency or clarity in terms of defining the objectives to be achieved, the issues to be addressed, including the particular needs of SMEs as well as the role and participation of the private sector, including NGOs, and of the bureaucracy. Moreover, government-private sector contacts are often highly personalized or opaque, which can lead to undesirable results.

16. Shortcomings in such interactions deprive the government of inputs for policy making and enterprises of inputs from the government for their strategic planning. Consequently, because of such shortcomings, it is not always evident that the process of policy and institutional development in support of SMEs in individual countries responds effectively to the needs and concerns of SMEs or takes sufficiently into account the difficulties or constraints faced by them.

17. This is partly a problem of the lack of effective representation of SMEs in the process of government policy-making. SMEs in fact often complain that, although they are in the majority, they have little influence on policy development concerning SMEs. Their views and experiences are often taken into account only selectively, if at all, in the policy-making process, including the preparation and implementation of development plans or structural adjustment programmes. Further, apart from poorly designed policies due to insufficient or wrong information, the lack of consultations with the private sector militates against the creation of trust-based relations between the government and private sector, which are essential for fostering development. 8/

18. Chambers of commerce, industry associations and various other forms of non-governmental business organizations exist in one form or another in most developing countries and in economies in transition. Often the government and the business community are represented jointly on the boards of these NGOs. They can play an important role in initiating and conducting government-private sector interactions. In Egypt, for example, the Federation of Egyptian Industries has organized a Government Relations Committee which represents all sectoral chambers and reviews the National Business Agenda. In their regular meetings with the Prime Minister, Committee members articulate policy positions and serve as the voice of the Egyptian industry. In other countries, such as in Canada, France, Indonesia, Malaysia and the United Kingdom, governments have established Ministries or Departments for Small Business or Enterprise Development to act as an interlocutor for the business community as well as a catalyst or a "lightning rod" for Cabinet-level policy development in support of SMEs.

19. However, it is seldom that all members of the private sector are represented in this dialogue. SMEs particularly often feel neglected or unable to participate due to various constraints, including lack of information, shortage of resources and work pressure, as well as various forms of discrimination against them. Moreover, the activities of the institutions

or agencies that organize this dialogue are sometimes only marginally related to enterprise development. This is particularly the case where the senior management is appointed, or where its appointment has to be sanctioned, by the government and where these institutions and agencies restrict their activities to the provision of administrative services.

20. A closer coordination of activities undertaken by the partners of the government-private sector dialogue would help to produce better results and strengthen the authority of the institutions involved. In Hungary, for example, great efforts have been made to advance the government-private sector dialogue on business cooperation programmes, including business incubators, as well as innovation and export programmes. But the coordination of programmes and institutions involved has proved to be difficult. The National Office of Small Business Development, which was established in 1990, did not seem to meet the expectations concerning its role as coordinator of the country's SME policies. A new department in the Ministry of Trade and Industry was given this responsibility, but it has been transformed into a Small Business Development Institute to monitor small business development. Thus, the Hungarian Small Business Association, founded as a not-for-profit organization in 1990, has emerged as the main umbrella organization for representing the interests of SMEs. Despite the intention to strengthen cooperation between the government and the social partners, including employers' organizations, SMEs still feel to be inadequately represented in the dialogue. 9/

A. Private sector organizations, particularly of SMEs, in government-private sector interaction

21. In order to be able to participate successfully in government-private sector interaction, it is important that the private sector partners, including SMEs, be well organized. Nationwide business organizations exist in most countries. Some of them are voluntary organizations, others are membership organizations grouping all registered enterprises. Several business organizations have been in existence for many decades. In other countries, particularly in transitional economies, genuine business organizations are of a more recent origin. 10/ Many of them are still in a process of consolidation, trying to strengthen their bargaining power and to improve their recognition by the government. In several countries, SMEs have tried to organize themselves by setting up their own SME sections within existing business associations or, even more radically, have tried to establish independent small business organizations. Such steps have often met with stiff resistance by established business organizations which are afraid of losing influence and membership fees.

22. The parallel existence of numerous business organizations that claim to engage in dialogue with the government and/or to support SMEs is common in most developing countries and economies in transition. Although the size of a country, the large number of SMEs and the wide variety of SME activities may necessitate the existence of multiple channels or levels of interaction, a heavy institutional superstructure, together with the proliferation and fragmentation of private sector representation, entails higher costs to SMEs and the risk of diminishing the effectiveness of government-private sector interaction. Moreover, the mandates of such organizations are often ambiguous, and they compete with each other, e.g. for members, funds, and

government contacts. In Egypt, for example, there are at least 30 government organizations and 107 non-governmental organizations which are involved in SME promotion. 11/ In Haiti, eight national bodies claim to represent the business sector.

23. In Sri Lanka, four organizations - the Sri Lankan Handicrafts Board (SLHB), the National Crafts Council (NCC), the Industrial Development Board (IDB), the National Design Centre (NDC) - have acted as conduits between the small-scale enterprises and relevant line Ministries. Such a multitude of organizations has been justified on the grounds that they can respond better to the different needs of SMEs which are engaged in the production of either industrial goods or handicrafts. However, in reality, it proves difficult for policy-makers to differentiate between these two groups of SMEs. Moreover, the basic problems faced by small enterprises in Sri Lanka have been fairly typical, irrespective of whether their production falls within one or another category. A lesson is that the integration of all small handicraft and industrial enterprises under the same organization or institution could help to achieve organizational "economies of scale" and to strengthen its role in a meaningful government-private sector dialogue. 12/

24. But there are also cases where the establishment of new SME business institutions appears to be justified. The emergence of such institutions, alongside established ones, in the same sectors or industries often signals dissatisfaction among the business community with the existing forms of representation, particularly its coverage in terms of membership, sectors and issues addressed.

25. Indeed, while in several countries, membership in industry associations or chambers of commerce is obligatory for all entrepreneurs that wish to have access to their services, in others some of the established private sector organizations discriminate against or exclude potential members not only on the basis of size of the business but also on religious, ethnic or gender grounds. Moreover, many of the organizations tend to focus primarily on preserving the interests of established entrepreneurs. The needs and problems of young and emerging entrepreneurs, including women entrepreneurs, who need targeted assistance particularly during the start-up phase, are often ignored by existing institutions. For example, in Zimbabwe, the Confederation of Zimbabwe Industries (CZI), including its numerous affiliated industrial associations, is a well-established independent, self-financed organization that enjoys a high level of credibility among both the Government and the business community. However, the relevance of these institutions, including their representativeness, is restricted due to the fact that it represents mainly larger companies with more than 50 employees, with little or no representation of smaller enterprises. Moreover, its activities are concentrated in the principal industrial centres, mainly the capital, and in a few subsectors of the manufacturing sector. 13/

26. A recent phenomenon is the emergence, sometimes with external assistance, of national NGOs, other than chambers of commerce or more business-oriented local NGOs, that strive to organize entrepreneurs and/or to act as a broker between the government and private sector. Many of these organizations are still in their early stages of development, which renders it difficult to ascertain their exact place in, and impact on, the relationship

between the government and the private sector. Since most of them focus largely on informal small-scale sector enterprises in both urban and rural areas, they could play a crucial role in better articulating the specific needs of small-scale entrepreneurs who exist in large numbers particularly in African and other LDCs, often without adequate representation. On the other hand, both governments and industrial enterprises seem to need some time to familiarize themselves with the framework of NGO interventions before they could tap the potential contributions of NGOs to the policy dialogue between the government and the private sector.

27. An efficient government service with sector-specific expertise is necessary for credibility with the private sector. It is also necessary in order to avoid the risk of "bureaucratic capture" by large firms or enterprises with strong political connections. However, against the background of deteriorating employment conditions in the public service, many governments and government institutions, particularly in LDCs, face increasing problems to retain able civil servants, particularly those who have established wide contacts with the private sector or who have accumulated business-related experiences. The outflow of talented civil servants to the private sector is undermining the capacity of the public administration to deal efficiently with business issues, while unsatisfactory employment conditions tend to undermine the morale in the civil service. A crucial issue related to the need for an efficient government service is the necessity of adequate follow-up to the decisions taken by government-private sector consultations.

B. Forms of government-private sector interaction

28. Although there is no standard form or prescription for government-private sector interaction, experiences of some East Asian countries, themselves far from following a uniform model, present several features and approaches that seem to be valid for the promotion of the government-private sector interaction in other countries as well. To begin with, the initial government-business dialogue in various East Asian countries was informal and focused on policies to protect infant industries and foster the development of technological capacities. Although in some countries, such as the Republic of Korea, SME issues gained formal recognition, as reflected in the Small Business Fundamental Act, 14/ it was mainly the larger enterprises which were involved in a dialogue with the Government. Over time, the nature and the scope of the government-private sector relationship has changed in virtually all countries and economies of the region. 15/ Governments have set up a framework for policy intervention, and the government-private sector policy dialogue has been structured and institutionalized as part of that framework.

29. Deliberation councils and other similar arrangements have become the central element in promoting government-business interactions and in obtaining inputs from the private sector for official policy-making. In Japan, for example, such deliberation councils are of two types: functional (for example, pollution or finance) and industry-specific (for example, automobiles or chemicals). Each council provides a forum for government officials and representatives from the private sector - business, labour, consumers, academics and the press - to discuss policy and market trends and generally to

exchange information. Government officials conduct hearings with interested parties, undertake research and prepare reports for the appropriate deliberation councils, where policy negotiations may take place. The reports are revised in the light of the deliberations and released to the public to explain the objectives of new policies. Final approval by Parliament is usually routine. Industrial associations have been important participants in the consultative process. In many cases, these associations are empowered by law to represent their constituents.

30. In the Republic of Korea, government-business consultations have also been used to solicit businesses' views on such matters as markets, regulations and potential plans and to include them as a critical policy component. As in the Japanese system, these consultations are basically of two types: functional and sectoral. Government officials also play an important role.

31. In Malaysia, the pinnacle of the consultative structure is the Malaysian Business Council, created in 1991, which is chaired by the Prime Minister himself and which includes more than 60 members from the Government, industry and labour. The MBC resembles the Republic of Korea's highly successful Export Promotion Council.

32. In Thailand, top government officials, particularly from the economic agencies, meet with business leaders from the chambers of commerce and industrial and bankers' associations in a national consultative committee, chaired by the Prime Minister himself. Provincial consultative committees have also been established to supplement the national committee.

33. In Singapore, the private sector, through its participation, for example, in the work of government statutory boards and ad hoc Government Advisory Committees, helps to review policies and programmes and to make recommendations for official consideration. In addition, the Government regularly invites chambers of commerce, trade associations and professional societies to submit their views on specific issues. A tripartite National Wages Council, including representatives from the Government, business and labour, has been established which fulfils several coordination functions, while simultaneously furthering business-labour cooperation. In Taiwan Province of China, consultation and coordination with SMEs is facilitated by middle- and lower-level officials of the Industrial Development Board, who make routine, informal visits to thousands of SMEs within their jurisdictions.

34. From an economic standpoint, deliberative councils facilitate information transmission. They enable the government to gather information about world markets, technology trends, and the impact of regulations domestically and abroad, to synthesize the information into an action plan, and to communicate the plan back to the private sector. Politically, these councils serve as proto-democratic institutions, providing direct channels for big business, labour and academia to the seat of power. Because the rules that govern an industry are effectively established within the council, every member is assured that the rules cannot be altered arbitrarily. With clear rules established, members can concentrate on market competition and not worry about others trying to curry special favours from the Government. It can also help to promote growth with equity, a particularly important objective for multi-ethnic societies.

35. The importance of deliberation councils can also be viewed from the perspective of their role in strengthening the quality of government-private sector cooperation. Given the many areas where there is a mutual interest in such cooperation, including, for example, skills, technological and infrastructure development, environmental protection and the promotion of inter-firm backward and forward linkages, the ability of the Government and the private sector to build up a confident and effective working relationship with each other assumes particular importance. The quality of such a working relationship might be a competitive advantage for a country in its own right in a globalizing and liberalizing world economy. In fact, it has been suggested that, in an increasingly interdependent world, competition among enterprises is often competition among different systems of government-private sector relationships. 16/

C. Promotion of policy coherence

36. A regular and effective government-private sector dialogue is essential for the flow of information, views and expectations from the government to the private sector and vice versa. It helps to build confidence and trust between government and its social partners by making government policies more predictable and understandable to the private sector and by allowing the latter to provide feedback to the government on policy measures. Above all, it facilitates the achievement of a coherent policy framework for enterprise and SME development.

37. The achievement of policy coherence implies not only the design of coherent policies but also clarity and consistency in their implementation, as well as an adequate response by the private sector. Thus, among other things, policies which have a bearing on entrepreneurship and the development of enterprises, such as policies relating to macroeconomic stabilization and functional issues such as taxation and business-related regulations will need to be consistent with sectoral and firm-level policies to develop new capacity or to achieve and maintain firm-level competitiveness.

38. Too often initiatives towards the development and promotion of SMEs are overruled by other government bodies or fall prey to actual or alleged constraints, such as fiscal pressure, monetary considerations or shortages of foreign exchange. 17/ However, since macroeconomic policies to achieve stability through high interest rates or to promote competition through trade liberalization may be damaging for SMEs, careful tuning and timing of such policies may be necessary, so that viable enterprises are given time to adjust, together with measures to facilitate their adjustment, including their access to essential inputs. Similarly, without creating business and consumer confidence by restoring fiscal control, the use of incentives to stimulate entrepreneurship and business start-ups may not be enough. Moreover, measures to facilitate structural change are necessary, including the development of infrastructure and of skills, if structural adjustment and liberalization are to lead to such change and thus to enhance the ability of firms and sectors to innovate and to adapt. On the other hand, support programmes for the development of SMEs need to be properly designed and contribute to productive activities, so that they will be fiscally neutral and not undermine macroeconomic stability.

39. There is also need for ensuring coordination, coherence and complementarity in the design and implementation of instruments for enterprise development. For example, adopting programmes to enhance the access of SMEs to essential inputs, including finance, complex machinery or imported components, will not be sufficient if there are no accompanying measures to help SMEs to obtain or use those inputs, including assistance in the preparation of viable loan requests or in the running of the machinery or the provision of access to foreign exchange.

40. In many developing countries and economies in transition, the issue of policy coherence needs to be seriously addressed. Shortfalls in creating a coherent policy framework are often related to weak institutional capacities. In countries where there is a multiplicity of official institutions dealing with SMEs, there is the additional problem arising from each of them pressing its own claims or vested interests. There is also the problem of the government trying to pursue conflicting objectives or attempting to do too much with too few resources, ignoring the role of private sector initiatives in this regard.

41. Incoherence in the formulation of macroeconomic and enterprise-specific policies is often more costly for SMEs than for larger enterprises. Further uncertainty on fiscal or monetary policies, for example, may stifle entrepreneurial initiative, while fundamental policy changes without sufficient lead time given to SMEs to adjust may even threaten their survival, as experiences of many developing countries and economies in transition with structural adjustment or trade liberalization measures have shown. In various instances, SMEs were subjected to competition before they were able to develop their capabilities, leading to plant closures and expansion of the informal sector. 18/ The higher cost of imported inputs due to devaluation and higher cost of credit due to liberalization measures have been prohibitively high for SMEs. 19/ All this has led to the growth of the informal sector in a large number of African countries.

42. While the primary responsibility for the design and implementation of economic policies and strategies rests with governments, policy coherence is best achieved when governments exercise their leadership role, set up an efficient inter-Ministerial consultative mechanisms and consult with the private sector. Governments may find it useful to seek inputs from the private sector at the beginning of the policy formulation process to make policy measures more practical and relevant, and not as an afterthought. In Gambia, for example, the Government has recently launched a new economic programme entitled "Vision 2020" 20/ which outlines its economic strategy to expand and diversify the country's productive base, mainly through expanded private sector activities. Several local businessmen, often on an individual basis, were able to contribute to the formulation of the strategic programme. But the government-private sector dialogue in the country may need to be further strengthened, particularly with regard to the formulation of policy frameworks for enterprise development, investment, trade and finance.

43. In light of the above and against the background of country experiences, the issues that may be addressed include:

(a) Based on your country experience concerning government-private sector dialogue, what form or structure does it take in terms of its objectives, its participants, the issues addressed and the frequency of meetings? Which mechanisms have proved to be successful, which ones have been a failure? What results have been achieved? How would success or failure be defined in this context? Why have some forms and structures been successful? Why have others failed? In light of these experiences, what lessons may be drawn regarding the effectiveness of such dialogue and the conditions for success?

(b) How have Presidential/Ministerial business councils changed the extent to which SME needs are being reflected in government policies and programmes? To what extent can their approach provide lessons for other countries?

(c) Few countries until recently have been aware of the need for coherence between macro and micro policies. What specific structures have been designed to ensure the coherence of macro and micro policies with respect to enterprise development? What difficulties are you encountering in attaining policy coherence for SME development?

(d) SMEs often argue that their voice is not heard when they are members of umbrella business organizations that include both large and small firms. What country experience might shed light on how to solve this problem of SME representation in umbrella organizations? Are SMEs more visible and do they impact more on policy design and implementation if they have their own organizations?

(e) Is there a national strategy for enterprise development? What are the main elements and to what extent does it address some of the issues raised in this paper?

IV. Support mechanisms and services for SMEs

44. The increased emphasis placed by all countries on the development of local productive capacity also extends to the issue of appropriate support mechanisms and structures for the promotion of enterprises, particularly SMEs. If policy and institutional development in support of SMEs is to be effective, the process has itself to be improved so that it becomes more coherent and more responsive to the real needs and concerns of SMEs.

45. Targeted assistance is needed if it is to be effective, and it can only be targeted if the government agency knows who the SMEs are and what their real needs and problems are. Thus, a profile of the SMEs and their particular needs and concerns may need to be established. Governments have also to decide on the type of support agencies and programmes which are to provide support services, including the question of "subsidiarity", i.e. who can do what best not only in terms of the public/private sector but also the national/local configuration. Moreover, support mechanisms and programmes need to respond to the diversity of firms involved and the types of problems faced by different categories of SMEs, ranging from subsistence or income-supplementing microenterprises operating in the informal sector to internationalized, technologically advanced SMEs.

A. The nature of SME support agencies

46. Many governments see advantages, particularly in terms of policy coherence, the allocation of resources, as well as the adaptation and dissemination of experiences and "best practices", in the development of a single development authority to oversee and to coordinate support programmes for SMEs. In fact, a number of governments have actively promoted the establishment of such centralized support agencies. However, administrative traditions and the power entrusted to local governments have also played a role in deciding on the kind of support agency to be established. Thus, particularly in countries which have a more federalistic structure, local governments have often taken initiatives to support locally- or regionally-based enterprises by, for example, setting up training institutions, organizing trade fairs and other promotional activities, creating regional banks, etc., while the central government mainly confines its role to the improvement of the macroeconomic, commercial and legal frameworks. South Africa, on the other hand, created a national SME promotion agency and combined national structures with a nationwide network of provincial bodies for consultations with the private sector and the provision of SME support services.

47. Enterprise support agencies can take different institutional and organizational forms. Some are parastatals, such as the Small Industry Development Organization in the United Republic of Tanzania. Others act as NGOs or autonomous organizations, like the Village Industry Service (VIS) in Zambia which promotes small-scale industries in rural areas. The status of an autonomous agency allows for a greater flexibility in operations, including the mobilization of funds. In addition to income-generating activities, VIS, for example, has been able to raise funds from other NGOs, bilateral and multilateral donors agencies as well as United Nations organizations. 21/ Likewise, SEBRAE of Brazil, a partially publicly-funded but privately-run institution, has also been able to raise funds from employers and users.

48. In other countries, SME support agencies operate as part of a Ministry, such as the Small Industry Support Programme in Indonesia, the Industrial Development Board in Sri Lanka, and the Indigenous Business Advisory Service in Gambia. The main advantage of being part of the government structure appears to be the availability of some minimum funds for these agencies through the budget. However, stringent government rules on, e.g., staffing, commercial activities, and contacts with other potential sources of funding may hamper their operational flexibility.

49. Although enterprises support agencies have been in existence in many countries for some time, their impact on new business formation and the survival and growth of existing firms has often been limited. They have been criticized for their bureaucratic nature, the absence of performance criteria for judging or stimulating their performance and their lack of effectiveness in responding to the needs of SMEs. Salaries have usually been too low to attract or keep experienced staff. Further, the rapport between staff and client has often been weak, stemming partly from the civil servant's traditional distrust of the "free-wheeling" entrepreneur and the businessman's fear of a government official prying too closely into his business affairs.

50. Another particular criticism is that, given the heterogeneity of SMEs, it is virtually impossible for the agency to encompass the range of expertise needed in a single institution to meet diverse needs. These shortcomings are partly due to the lack of well-designed policies and strategies for SME promotion in most countries. Moreover, the fact that industrial policies have very often focused heavily on the growth of large-scale manufacturing firms has also had adverse effects on the promotion of SMEs. 22/ Israel, however, has overcome this problem by creating a network of Small Business Development Centres which are NGOs and service different kinds of entrepreneurs: new immigrants, women who must work at home, etc.

51. Most of the SME support services are "supply-driven", mainly providing business support services in areas such as advisory services, training, finance, advertising, marketing, export consultancies, etc. They try to cover as wide a spectrum as possible in terms of enterprises and sectors. However, most of the successful SMEs have grown on a demand-driven curve. They started in a certain sector or with certain niche products, attracting customers among larger enterprises, both domestic and abroad, and then branched out from their original sectoral or product base. This development has been supported by their customers, typically large firms or subcontractors, which provided market access, know-how and technical help and even finance. The customers also centred their assistance around their particular needs and around problems that emerged in the SMEs while they were working to fulfil orders. Many government support institutions have not yet incorporated demand-driven elements in their programmes. 23/

52. However, these criticisms are not sufficient arguments on their own for doing away with a government support structure for SMEs. Rather they are arguments for improving their organization and functioning. Such improvements may include refocusing their role on essential functions like policy development, streamlining their organization and attracting better qualified staff, supplementing or supporting private sector activities in areas where the private sector has better expertise rather than duplicating them, and coordinating with specialized institutions in the provision of specialized services to SMEs. Moreover, the role of the government is not necessarily to provide the advisory, consultancy or technical assistance services, but rather to stimulate the private sector to take initiatives and to provide some financial support where necessary, leaving intermediaries to deliver the services. Institutions most commonly providing such services might be business associations established by groups of enterprises, professional societies in fields such as accounting or engineering, ad hoc organizations established jointly by government agencies and business groups, and international organizations.

B. The promotion of SME support agencies

53. In order to promote SME support agencies and to stimulate the supply of appropriate support services, governments have undertaken various measures. These include direct financial support, e.g. financial assistance to overcome a shortage of venture capital or seed money to establish venture capital funds; fiscal and credit incentives, e.g. exemption from import duties on equipment, tax exemptions on royalties, accelerated depreciation schemes or subsidized loans; and deregulation, e.g. regulatory reform in order to remove

the boundaries between different services. For example, Egypt's Fund for Social Development has provided considerable support for the micro-enterprise sector particularly in helping these entrepreneurs do a business plan and facilitating loans from the regular banking system to enterprises which cannot provide collateral. This measure could remove one important obstacle to growing microenterprises into SMEs. Other components of the strategy to promote the supply of such services include incentives for the "externalization" of locked-in service activities, and the establishment of training centres for the training of trainers.

54. An interesting example of SME support structures is to be found in Singapore. There are over 60 support programmes for enterprises, regardless of size. These provide support for various stages of enterprise growth, from start-up to expansion to overseas activities. They range from low-cost financing, tax incentives, business development, marketing, design, technology adoption, standards upgrading, productivity improvement and computerization to expanding operations abroad. These support programmes are coordinated by the Economic Development Board through its Enterprise Development Division, upgraded from a Small Business Bureau as its activities expanded to keep up with the growth of local enterprises, both in size and in number. These support programmes are administered by the Enterprise Development Division itself or in cooperation with one or several specialized institutions dealing respectively with, inter alia, automation applications, science and technology, information technology, productivity promotion, trade and computerization, as well as standards and industrial research (which also provides incubation facilities for start-up companies). In the case of the last two areas, support is provided independently by the specialized institutions or by them in association with universities.

C. Principles for the development of support programmes for SMEs

55. The choice of a centralized agency or a multi-agency approach and the scope of the activities of agency authorities are a function of the diversity of country situations, for example in terms of their levels of economic development, the commercial and regulatory environment, or the existing business culture. However, some general principles may be identified in defining an overall policy framework for the development of support programmes for SMEs.

56. The establishment of SME support agencies and programmes need to go in parallel with efforts to improve the policy, legal and regulatory environment in which SMEs operate. This would imply, among other things, reducing subsidies and other policy measures which favour large enterprises and discriminate against SMEs, simplifying regulations and administrative procedures for business start-ups and development and enacting new legislation to deal with gaps or inconsistencies in business laws. In the final analysis, improving such an environment may be more beneficial for SME development than specific support programmes. In Norway, the Government, recognizing the constraining nature of the regulatory environment for business development, has established a Business Legislation Committee to review on an ongoing basis the regulatory framework and make proposals for simplified administrative rules and other changes for stimulating business activity. An addition, a new Competition Act has been enacted to enhance competition. In China, the very

act of deregulating employment by allowing self-employment has released the floodgates of entrepreneurial energy and led to a rapid growth of SMEs established by peasants and urban dwellers. Other measures in China include the simplification of registration procedures for commercial and industrial enterprises and the relaxation of State controls on mineral resources (for example, coal). These have led to the establishment of SMEs not only in commerce and services, but also in industry and mining (with small rural and town collieries accounting for one third of total coal output). Thus, improvements in the regulatory framework, can by themselves serve as policy induced incentives to SME development. By opening up markets to competition, they also encourage the operation of market-based incentives. 24/

57. As a matter of principle, support programmes should be market-based and demand-driven, i.e. they should tap and build on the expertise, capabilities and resources available in the private sector and thus complement rather than duplicate them. They should also be the outcome of close cooperation with the private sector, thus reflecting the actual demand by the business sector and the potential of the government to supply such services. The application of user charges, which may be introduced progressively where necessary, helps to gauge demand and to promote sustainability.

58. The approach will obviously depend on the level of development of market institutions or networks. In many economies in transition, for example, where market mechanisms and business support services are relatively weak, the agency may have to assume a more important role, with outside help, if necessary, until private sector capabilities are developed. Further, in those countries, the training of trainers, for example of business and management skills, may be needed in order to create the necessary multiplier effects in a vast programme of capacity-building for business development.

59. Priority would also need to be given to enhancing the availability and efficient utilization of essential inputs commonly needed by SMEs, including finance, land, physical facilities and equipment. This would imply, among other things, improving SME-targeted credit facilities by the agency and by agency-supported private intermediaries, changing zoning regulations that tend to restrict the access of SMEs to well-located sites, providing common facilities and making equipment and spare parts more readily available to SMEs. Efficient utilization of inputs through technical assistance can help to reduce costs and may be as important as the financial costs.

60. Support programmes should be designed to help promote inter-firm linkages among SMEs and between them and larger firms so as to improve skills, business information and production, marketing and sales opportunities of SMEs through inter-firm and market networks. This may require, among other things, establishing a subcontracting exchange or a network facilitator and having the SME development agency work closely with the investment promotion agency with regard to inter-firm linkages with foreign firms. Facilities, such as incubators, for promoting collective efficiency and synergies between firms, including firms from other countries, may also be created, as in Singapore, for example.

61. Support programmes may also serve as an incentive for enterprises, particularly SMEs, to better organize themselves and to register themselves with the authorities. In Zimbabwe, for example, the Small Business Support Unit of the Zimbabwe National Chamber of Commerce (ZNCC) encourages participants of training, advisory and consultancy services to belong to the ZNCC or to other business organizations, so as to facilitate networking among entrepreneurs and the sharing of experiences among SMEs of the same trade. Training programmes in other countries also tend to discourage the participation of entrepreneurs from unregistered firms or to give preference to registered firms in their information, credit, marketing and other advisory services. 25/

62. SMEs have often flourished in countries where governments have encouraged relatively open and competitive markets. In such an environment, firms in the same line of business compete with each other on a more equal footing. Just as important in this environment, firms in different fields can form complementary relationships. Where interdependence between suppliers and customers is allowed to develop freely, many of the supporting services will be provided by other firms and will no longer need to be provided by the government. The larger firms which depend on SMEs to become efficient suppliers of specialized components or services for their production processes will themselves have the incentives to provide technical help and training to the SMEs in order to increase their efficiency. In Taiwan Province of China, large firms have provided trade credit and large-scale loans to their SME partners, thus partially offsetting the discriminatory impact of government-induced distortions against SMEs in the financial markets. Studies of African and other countries show that inter-firm or market networks have helped to provide business support services highly valued by SMEs.

63. An issue for debate is whether support programmes should be applied to all enterprises, regardless of size, or whether and to what extent they should be targeted at SMEs. There seems to be some justification for arguing that a "level playing field" should be created for all enterprises, regardless of size, and that, if policy interventions are needed, they should be directed at eliminating the bias in favour of large enterprises, for example subsidized credit or special foreign exchange allocations for such enterprises, rather than being packaged specifically for SMEs.

64. However, in practice, things may not be that simple. Many SMEs, notably small and microenterprises, may not be able to compete on equal terms, particularly with regard to access to finance or information, and some specific additional measures may be needed in order to help them. Even where such support programmes are intended for all enterprises, as in Singapore, they started as SME-targeted programmes; the coverage has been widened by raising the eligibility threshold because of the need to respond to the requirements of growing local enterprises. Further, if public administration is poor or corrupt, if lump-sum taxes or licence fees are high or if the cost of capital is high or often at the mercy of bad macroeconomic management, the cost of administrative compliance or of raising working capital will be disproportionately higher for SMEs than for large enterprises. They may prove to be prohibitive or even fatal for some SMEs.

65. Since the provision of development services to enterprises can be costly, mechanisms for the long-term financial sustainability of such services and related institutions are important. Obviously it would be unrealistic to expect smaller enterprises to pay cost-covering user fees, particularly during their start-up phase. It may also be argued that such services should be provided at a moderate cost and that any subsidization may be offset by subsequent increased tax revenue. However, there is a need to ensure that the delivery of such services is cost-effective. Thus, the subsidization of business services needs to be phased out as the recipient enterprises become more viable. User fees need to be charged at a level that reflect the real market value of the services provided. As regards business advisory services for SMEs starting a business for the first time, the provision of vouchers which entitle emerging entrepreneurs to a fixed number of consultancies could be an appropriate means to keep costs of the support programme low and to prevent abuses. A voucher scheme for training has also been introduced in Paraguay. Since voucher holders are able to exercise a choice, the training institutes are obliged to become more responsive to their needs.

D. The role of private sector service providers

66. Apart from support services provided by enterprise organizations for their members free of charge or at a token price, many support activities can be offered by the private sector on a commercial basis. This may include support services in areas such as advisory services, market research, financial services and accounting, legal issues and training. As a general rule, as enterprises and economies develop, a greater proportion of the support services can be provided on a commercial basis, including those services that have originally been provided by enterprise organizations to their members at subsidized prices.

67. Private sector providers of SME support services have the advantage of being more cognizant of market demand and specific SME needs than civil servants. They are also often capable to deliver higher-quality services with greater flexibility and at lower costs. Research institutes, technology centres, and universities can also fulfil a useful role in assisting SMEs, primarily when specialized bodies have been created with organizational and financial independence.

68. Such institutions may need to be established in areas like automation, productivity improvement, standards and industrial research, and science and technology as in Singapore. These specialized institutions may also be linked to research programmes of universities. Apart from undertaking research on particular industrial technologies or industries, including their human resource development implications, they can help to disseminate information where inter-firm networks may be deficient, for example due to foreign firms being unwilling to share critical information with local companies. Thus, the central development agency and specialized institutions may help to compensate for "market failures". However, they need to be properly staffed and motivated, so as to avoid "government failures".

69. Based on concrete country experience, the discussion may focus on the following issues:

(a) What types of support agencies and services for SMEs have been established? What lessons may be drawn from their experiences regarding the questions of outreach, efficiency, effectiveness and sustainability? How is the issue of "subsidiarity" addressed?

(b) Women and emerging entrepreneurs often have needs that are different from those of other entrepreneurs. What mechanisms have you developed for taking their special needs into account? How effective have these been?

(c) Some governments have established SME support agencies within government structures. What are their main functions? How effective have these agencies been as channels for a two-way flow of information between government and SMEs? What are the pros and cons of a centralized agency versus a multi-agency approach? What other structures might effectively serve such a purpose?

(d) Targeted support to microenterprises is often provided in terms of, for example, help for preparing business plans or for improving their access to finance. Has this kind of assistance enabled microenterprises to grow into SMEs? What are the particular problems that support agencies encounter in providing assistance to microenterprises?

(e) Since the provision of development services to enterprises can be costly, mechanisms for the long-term financial sustainability of such services and related agencies are important. What is your experience concerning, for example, user fees, scaled fees, voucher programmes and other cost-recovering mechanisms?

(f) Various support services can also be provided on a commercial basis. How do you see the role of the private sector in providing such services? What is your experience with private sector "self-help" support agencies and services for SMEs? How are they integrated in the overall SME support programmes and measures?

Notes

1/ See Report of the Commission on its first session (TD/B/44/2-TD/B/COM.3/4), annex I, subpara. 3 (i).

2/ Ibid., para. 4.

3/ For a detailed discussion of the role of SMEs in development see: UNCTAD: Creating an enabling development for the development of enterprises, particularly small and medium-sized enterprises. Report by the UNCTAD secretariat (TD/B/WG.7/3), Geneva 1995.

4/ See: UNCTAD: The changing nature of enterprises and competition and the implications for the formulation of an enterprise development strategy (TD/B/COM.3/2), Geneva 1996.

5/ See: Government of Norway: Country contribution to the UNCTAD Ad Hoc Working Group on the role of Enterprises in Development, Geneva 1995.

6/ See: Summary of the main points made in the discussions of the first session of the Ad Hoc Working Group on the Role of Enterprises in Development, UNCTAD, Report of the Ad Hoc Working Group on the Role of Enterprises in Development on its first session (TD/B/WG.7/4), Geneva 1995.

7/ See: DSE: Report of the International Round Table "Promotion of the Private Sector and the Role of Government", Bonn/Bad Godesberg, 6-9 February 1996.

8/ See: J. Humphrey, H. Schmitz: Trust and economic development. IDS Discussion Paper 355, University of Sussex 1996.

9/ See: Z. Roman: The role of the State in creating an enabling environment for the promotion of SMEs. Notes on the Hungarian Experiences. Geneva 1995 (mimeo.).

10/ See: ECE: Small and Medium-Sized Enterprises in Countries in Transition. Geneva 1996.

11/ See: Federation of Egyptian Industries: Directory for the governmental and non-governmental organizations in the field of small and medium-sized enterprises in Egypt. Cairo 1996.

12/ See: ILO: Study on government agencies providing assistance to the handicraft and small-scale industry sectors in Sri Lanka. Geneva 1991.

13/ See: Zimconsult: Feasibility study for establishing a fund for innovation and development. Harare 1996 (mimeo.).

14/ Law No. 1840 of 6 December 1966, and the following amendments: Law No. 2996 of 31 December 1976, Law No. 3125 of 5 December 1978, Law No. 3650 of 31 December 1982. Other legal acts that recognize the importance of SMEs and are aimed at their promotion include the Small and Medium Industry Promotion Act (1982), the Small Business Cooperative Act (1961 and subsequent amendments), the Small Business Transaction Coordination Act (1982), the Small Business Sub-Contracting System Promotion Act (1975 and subsequent amendments), the Small Business Products Procurement Act (1981), the Small Business Enterprise Creation Promotion Act (1986), the Act of Special Measures for the Promotion of Managerial Stability and Restructuring of Small Businesses (1989) and the Fair Sub-Contracting Transactions Act (1984 and subsequent amendments).

15/ See, for example, the evolution of small business legislation in the Republic of Korea, as listed in the previous footnote.

16/ See: I. Ul Haque: International Competitiveness - Interaction of the Public and Private Sectors. World Bank EDI Seminar Series. Washington, D.C., 1991.

17/ See: H. Kiaratu: Overview of SMEs Development in Tanzania. Geneva 1995 (mimeo.).

18/ In Ghana, for example, the textile and garment sector, i.e. industries mostly dominated by SMEs, was one of the hardest-hit by these measures, contributing substantively to the drop of the manufacturing production indices of 22 per cent in 1992 below the 1979 reference level. In Kenya, while the formal manufacturing sector declined during the economic adjustment process, the share of the informal sector in total employment increased from 18 per cent to 27 per cent between 1986 and 1992. See: O. Boeh-Ocansey: Small industries and structural adjustment. In: Small Business Development, vol. 6, No. 2, June 1995.

19/ For example, in Gambia nominal costs of business loans amount to about 25 per cent. Given an annual inflation rate of less than 2 per cent, the real interest rate for business loans of more than 20 per cent is prohibitive for small-scale entrepreneurs, not taking into account stringent collateral requirements enforced by commercial banks.

20/ See: Goverment of the Gambia: The Gambia incorporated ... Vision 2020. Banjul 1996.

21/ See: S.N. Kapaku: The role of NGOs in the promotion of SMEs. The case of the Village Industry Service in Zambia. (UNCTAD/ITE/EDS/Misc.3) Geneva, 1997.

22/ See: M. Gibb; G. Manu: The design of extension and related support services for small-scale enterprise development. International Small Business Journal 8.3.

23/ See: J. Tendler; M. Alves Amorim: Small firms and their helpers: lesson on demand. World Development, vol. 24, No. 3, 1996, pp. 407 ff.

24/ See UNCTAD, op. cit., para. 42.

25/ See: M. McPherson; C. Liedholm: Determinants of Small and Micro Enterprise Registration. Results from Surveys in Niger and Swaziland. World Development, vol. 24, No. 3, 1996, pp. 481 ff.